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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Pay Telephone	)	**CC Docket No. 96-128**
Reclassification and Compensation	)	
Provisions of the Telecommunications	)	
Act of 1996	)	

COMMENTS OF SPRINT CORPORATION

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SUMMARY

It should be clear from the two court reversals that have already occurred in this docket that the Commission needs to step back and fundamentally rethink its approach to payphone compensation.

If the Commission wants to adhere to a market-based approach, the only way to do so is by adopting a caller pays plan that would permit PSPs to collect (if they wish to do so) directly from calling parties for the use of their phones for access code and subscriber 800 calls. The Commission adopted this market-based approach for local calls – which account for 70% of the calls made from a typical payphone – and there is no reason why it could not be adopted for these other types of calls as well. Neither the Commission's prior rejection of the caller pays approach, nor the Court's affirmance of that decision, would preclude the Commission from adopting a caller pays plan today. The complex burdens placed on IXCs in administering the present carrier-pays approach and the attendant transaction costs that ultimately must be borne by consumers would be eliminated by adoption of a caller pays plan. A caller pays plan also would avoid the continuing drain on the Commission's resources from resolving billing disputes that will arise, and from relitigating periodically the prescribed level of compensation.

After two court reversals, the Commission should not seriously entertain an attempt to construct a market-based rate for carrier-paid compensation where no market in fact exists. Indeed, the very notion of a prescribed "market-based" rate is a contradiction in terms.

Rather, if the Commission declines to adopt a caller pays plan, its only alternative consistent with logic and past precedent, is to adopt a cost based rate, based on the costs of an efficient PSP, not on industry average costs or on the costs of high-cost, inefficient PSPs. The record already contains sufficient data to make such a prescription. Using conservative assumptions, a cost-based rate should be no higher than 14.3 cents per call.

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In the Matter of	)	
	)	
Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996	))))	**CC Docket No. 96-128**

COMMENTS OF SPRINT CORPORATION

Pursuant to the Common Carrier Bureau's June 19, 1998 Public Notice herein (DA 98-1198), Sprint Corporation hereby submits its views on the actions the Commission should take on remand from the United States Court of Appeals for the District of Columbia Circuit.[1] The Public Notice states (at 3) that the record in this proceeding will include the comments and reply comments in response to the previous remand in this docket,[2] and the reconsideration pleadings relating to the Second Report and Order adopted in response to the earlier remand. Accordingly, in these comments Sprint will endeavor to avoid unnecessary duplication of its earlier argument in those filings.

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[1] MCI Telecommunications Corporation, et al. v. FCC, No. 97-1675, May 15, 1998 ("Payphone II"). All subsequent references to that decision will be to pages of the slip opinion. That decision reversed and remanded the Second Report and Order herein, 13 FCC Rcd 1778 (1997).

[2] Illinois Public Telecommunications Association v. FCC, 117 F.3rd 555 ("Payphone I"), clarified, 123 F.3rd 693 (D.C. Cir. 1997), reversing the Commission's Report and Order, 11 FCC Rcd 20541 (1996) and Order on Reconsideration, 11 FCC Rcd 21233 (1996) in this docket.

I. THE COMMISSION SHOULD STEP BACK AND RE-THINK ITS APPROACH TO PAYPHONE COMPENSATION

Sprint urges the Commission to take a step back and re-think, from square one, its whole approach to payphone compensation. The Commission's previous orders in this docket have been riddled with illogic and shifting rationales. In its Notice of Proposed Rulemaking, 11 FCC Rcd 6716 (1996), the Commission unequivocally proposed to base compensation for access code and subscriber 800 calls on costs (yet failed to require PSPs to submit comprehensive cost data). The Commission's first Report and Order (11 FCC Rcd at 20577) rested the compensation rate prescribed therein on costs and rejected "market-based surrogates," but used a deeply flawed measure of costs. (Specifically, it assumed that the costs of these coinless calls were identical to an arbitrarily selected "market" rate for local coin calls.) At the same time, the Report and Order elsewhere (e.g., 11 FCC Rcd at 20567) spoke in terms of using the market to set the compensation rate. The Order on Reconsideration affirmed the findings of the Report and Order on costs (11 FCC Rcd at 21268), but in other respects placed more weight than the Report and Order on the notion of market-based rates (id. at 21237, 21266-67). The Second Report and Order disclaimed any reliance on costs, choosing instead to rest solely on a "market-based" rate (e.g., 13 FCC Rcd at 1818, 1820, 1828). However, the Commission then adopted a result that was wholly illogical by finding that a market rate for carrier-paid compensation for coinless calls could be determined by subtracting the cost differences between coin and coinless calls from an assumed market-based rate for local coin calls.

The Commission's first two efforts to set a compensation rate for access code/subscriber 800 calls were not well-received by the Court of Appeals. In Payphone I, the Court stated (117 F.2d at 564) that the Commission's reasoning "epitomizes arbitrary and capricious decisionmaking." And in Payphone II, the Court (at 5) found the Commission's approach in the Second Report and Order "plainly inadequate," "unreasoned" and "utterly unhelpful." It may not be unprecedented for the Commission to have been reversed twice in the same administrative proceeding.[3] It may well be unprecedented, however, for the second reversal in the same case to have come so swiftly – just one week after oral argument. It is obvious from Payphone I and Payphone II – all the more so to anyone who attended oral argument in Payphone II – that the Commission's approach to payphone compensation for dial-around and subscriber 800 calls to date is deeply and fundamentally flawed, and cannot be sustained if all the Commission does is to make new jury-rigged findings to support its previous result. Yet, Sprint is concerned, from the questions framed in the June 19 Public Notice, that this is the path the Commission is heading down again. Most of the questions seem designed to elicit information that would enable the Commission to support its previous approach. It asks for other market-based approaches and cost data almost as an afterthought.

Whatever result the Commission reaches in this second proceeding on remand, the Commission should expect that its decision will again be appealed, either by IXCs,

[3] By some counts, the Commission has been reversed three times rather than twice. In the wake of the Bureau's Public Notice (DA 97-1673, released August 5, 1997), interpreting Payphone I as having left the rates established in the Report and Order in effect, the Court granted motions to clarify that on the contrary, the Court's decision in Payphone I vacated the interim and "permanent" rates established in the First Report and Order. See 123 F.3rd 693 (D.C. Cir. 1997).

PSPs or both sets of parties, simply because of the economic stakes at issue.[4] Having twice been reversed in the same proceeding, the Commission can expect the Court to review its next order with somewhat greater than usual scrutiny. As the D.C. Circuit has observed:[5]

> At the same time, we must recognize the danger that an agency, having reached a particular result, may become so committed to that result as to resist engaging in any genuine reconsideration of the issues. The agency's action on remand must be more than a barren exercise of supplying reasons to support a pre-ordained result. Post-hoc rationalizations by the agency on remand are no more permissible than are such arguments when raised by appellate counsel during judicial review.

In view of the Court's obvious dissatisfaction with the Commission's prior efforts, any attempt by the Commission simply to shore up its previous approach, as the questions in the Public Notice suggest may be its intent, may convince the Court that that the Commission is too committed to its previous result to genuinely reconsider these issues again.

It is important for the Commission to forestall yet another reversal by adopting a sound, logical compensation plan that will survive the heightened scrutiny the Commission can expect to face in the next appeal. First and foremost, the Commission has a statutory obligation to develop a lawful compensation plan. Second, the industries that presently pay and receive such compensation need finality and certainty so that they all can plan and manage their businesses accordingly. Third, continued litigation imposes costly and unnecessary drains on the time and resources of both the Commission and the

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[4] The Second Report and Order requires carriers to pay in the neighborhood of $1 billion in annual compensation to payphone service providers (PSPs).

[5] Food Marketing Institute v. ICC, 587 F.2nd 1285, 1290 (D.C. Cir. 1978).

interested parties. This is the third consecutive summer in which counsel for IXCs, PSPs and other affected parties (such as the paging industry) have been writing comments on payphone compensation. In addition to the resources consumed by the basic compensation issue, this docket is rife with other pending issues that have yet to be addressed.[6] The Commission and the industry need to move on. Finally, the Commission should be concerned that yet another judicial reversal in this docket could have spillover effects on review of Commission actions in other proceedings. In Sprint's view, the best way for the Commission to dispel this possibility is to take a fresh and objective look at its entire approach to payphone compensation for access code and subscriber 800 calls.

II. THE CALLER PAYS SYSTEM IS THE ONLY TRUE MARKET-BASED COMPENSATION SYSTEM

From the outset of this proceeding Sprint has urged that if any compensation is to be prescribed at all,[7] it should be based on the costs of an efficient PSP. And Sprint will discuss cost-based compensation further in the next section of these comments. Nonetheless, Sprint is mindful of the Commission's preference for a market-based

[6] The Commission has not yet acted on the interim compensation plan covering the period November 1996-October 1997 that was overturned in Payphone I. In addition, there are numerous requests pending for Bureau reconsideration or Commission review of various actions taken by the Bureau under delegated authority.

[7] As Sprint pointed out in its initial filing in this docket (July 1, 1996 Comments at 17-18) the payphone industry has grown without any revenues from the types of calls at issue (and, it might be added, with lower revenues from coin calls than PSPs now receive), thus suggesting that PSPs were already fairly compensated for all calls from their payphones. The PSP industry has never shown in this docket that in fact an efficient PSP would need any additional revenues to cover its costs. Furthermore, the handling of access code/subscriber 800 calls imposes only de minimis marginal costs on PSPs – just a minor amount of wear and tear on the keypad and handset.

approach and of the fact that the Court in Payphone II (at 6) held open the possibility that a market-based rate could satisfy the statutory requirement for "fair" compensation.

The only true market-based approach is a "caller pays" plan that would permit the PSP, if it wishes to do so, to assess a charge directly on the caller for the use of payphone for an access code or subscriber 800 call.[8] It is, after all, only the party placing the call from a payphone that decides to use a particular payphone at a particular location and thus imposes whatever costs there may be on the PSP for using the PSP's equipment. And only the caller is in a position to decide whether the PSP's charge (if any) for the use of its phone for access code and subscriber 800 calls is justified by the convenience of being able to use that phone, instead of going to another site in hopes of finding a less expensive payphone or waiting to use a residential or business phone to place the call. On the other hand, if a PSP perceives that its charges (if any) for such calls are higher than a profit-maximizing level because too many callers are avoiding the PSP's phones, the PSP can adjust its rate to the profit-maximizing level its consumers – the calling parties – are willing to pay. Thus, the caller pays system sets in motion the forces that could enable a market rate to be established. This is the very same compensation plan the Commission adopted for local calls – which account for 70% of payphone-originated calls – and there is no reason why this approach would not work for access code and subscriber 800 calls as well.

Neither the Commission's previous rejection of a caller pays plan for access code and subscriber 800 calls, nor the Court's affirmance in Payphone I of that rejection,

[8] Such a charge could be collected either by a coin deposit or a charge to a credit or debit card.

would preclude the Commission from revisiting this issue and adopting a caller pays plan today. In its Report and Order (11 FCC Rcd at 20585), the Commission advanced three reasons for rejecting caller-pays. First, the Commission found that a caller pays plan shared the same characteristics as the "set use fee," which the Commission declined to adopt (id. at 20584-85) in lieu of a "carrier pays" approach because of the high transaction costs that would result from the large number of persons that would be charged the fee on their telephone bills.[9] As it happens, because, under the carrier pays plan, the IXCs recover their costs by billing a surcharge to the party responsible for paying the underlying call, there is no practical difference, in terms of transaction costs, between the set use fee and carrier pays approaches. In any event, the Commission's perceived problem with the set use fee – the transaction costs of the multiplicity of bills involved – does not apply at all to the caller pays system. No tracking and billing processes are necessary at all if the caller simply deposits coins in the payphone before making a call. The Commission acknowledged (11 FCC Rcd at 20585) the defect in its set use fee analogy by recognizing that depositing coins to make a subscriber 800 call would not be more burdensome than a local coin call and would involve fewer transaction costs than a billed charge.

The second reason the Commission gave (id.) for rejecting a caller pays plan was an unsupported finding, made without citation to any record evidence and instead only quoting an unsupported statement in its NPRM (11 FCC Rcd at 6730), that it "would appear to unduly burden many transient payphone callers by requiring them to deposit

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[9] See NPRM, 11 FCC Rcd at 6729-30, for descriptions of the "set-use fee" and "carrier-pays" approaches.

coins... ." To be sure, requiring callers to have coins (or a credit card) when placing such calls would mean a one-time change in consumer habits, and Sprint would expect that the industry would cooperate with the Commission in educating consumers about this change. Undoubtedly, a caller pays plan could prove inconvenient to particular consumers at times, just as not having enough coins for a local coin call can be inconvenient. Sprint wishes to emphasize, however, that callers would not need to have either coins or credit cards to place emergency calls. In any event, the Commission accepted coin deposit as a reasonable means of compensation for 70% of all calls made from payphones – local coin calls – and once consumers get used to this one-time change in calling patterns, the burden should be neither unusual nor undue.

The final reason given in the Report and Order (11 FCC Rcd at 20585) for rejecting the caller pays approach was concern that it might run afoul of §226(e)(2).[10] Sprint does not believe that §226(e)(2) is a bar. That provision directs the Commission to "consider the need to prescribe compensation (other than advance payment by consumers) for owners of competitive public pay telephones for calls routed to providers of operator services... ." That language is hardly a bar to Commission reliance on such advance payment as a means of fair compensation. In its initial NPRM implementing that provision, the Commission observed that if it declined to prescribe compensation, as was within its discretion under that provision, payphone owners would be free to charge

[10] Sprint notes that in the Reconsideration Order (11 FCC Rcd at 21275) the Commission characterized its Report and Order as having found that TOCSIA "prohibited us from prescribing that approach for interstate access code calls...", whereas in the cited portion of the Report and Order, the Commission merely concluded that "such an approach would contradict the Congressional intent and possibly the plain language, of §226(e)(2) of the Act" (footnote omitted).

the calling party for the use of their phones.[11] Here, if the Commission adopted a market-based caller pays plan, it would not be "prescrib[ing] compensation, and thus §226(e)(2) is not even implicated.

In that regard, nothing in 276(b)(1)(A) requires the Commission to "prescribe" compensation. Instead, this provision merely requires the Commission to "establish a per-call compensation plan to ensure that all payphone service provider are fairly compensated for each and every completed intrastate and interstate call using their payphone... ." This "plan" could consist simply of allowing payphone providers to choose whether and how much to charge calling parties for various types of calls (just as the Commission allows PSPs to choose whether and how much to charge calling parties for the local calls that make up 70% of total payphone-originated calls). If a market-based approach can be used to determine "fair" compensation, then a plan that leaves it to market forces to determine whether and how much PSPs collect for particular types of calls is sufficient to meet the duty imposed on the Commission by §276(b)(1)(A).

The further reasons given by the Commission in its Reconsideration Order for rejecting caller pays are likewise without merit. The Commission first noted (11 FCC Rcd at 21276) that §226(c)(1)(C) would require PSPs to charge the same amount for a call via the presubscribed OSP as it charges for dial-around operator services calls, but neglected to explain what is wrong with that. If the PSP is concerned about the total charge to the customer for making 0+ calls, that is simply another factor it can take into account in deciding an appropriate market-based rate for all such calls. Alternatively the PSP, considering its revenues from caller pays, could agree to a lower level of

[11] Policies and Rules Concerning Operator Service Access and Pay Telephone

commissions from the presubscribed OSP, or could lower its own charges for the 0+ call in cases where the PSP also functions as the operator services provider.[12]

Second, the Commission (id.) pointed to §228(c)(7) as evidencing a Congressional intent that calling parties should avoid being charged when they access subscriber 800 numbers. However, as the Commission acknowledged (id.), "this provision does not expressly apply to PSPs… ." That being the case, the Commission cannot presume that this provision reflects a Congressional intent for situations Congress chose not to address in the legislation. Furthermore, what is involved here is not a charge to the public for 800 service, rather it is simply a rental charge for use of a payphone to make a telephone call. Such a charge is far outside the bounds of §228(c)(7).

Finally, the Commission (id.) stated that it would be unduly burdensome to adopt a partial caller pays plan so that certain subscriber 800 calls, such as calls to a paging service, would be subject to coin deposit requirements, while relying on a carrier-pays approach for other calls. Although the Commission did not elaborate on what those burdens and costs would be, in any case, there would be no such burdens with a pure caller pays approach.

In affirming the Commission's rejection of the caller pays approach, the Court in Payphone I did not make any determinations that would preclude the Commission from adopting a different result this time around. The Court did not rely on any statutory prohibition against a caller pays plan, but instead merely held that the Commission had reasonably exercised its discretion in adopting a carrier pays system instead of a caller

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Compensation, 6 FCC Rcd 1448, 1450 (1991).

[12] Generally, where "smart" payphones are used, the PSP does act as the operator services provider for all calls that do not require the intervention of a "live" operator.

pays system. This affirmance in no way precludes the Commission from adopting a different result so long as the Commission adequately explains its reasons for its change in course.[13]

Plainly, the Commission can provide a reasoned basis for reversing its earlier rejection of a caller pays plan. First, it should be apparent to the Commission that the administration of a carrier pays plan is far more complex than the Commission envisioned when the Commission first adopted such a plan. Scores of carriers must keep track of calls originating from roughly two million payphones, must verify the ownership of those phones, and must remit compensation to in excess of a thousand individual PSPs. In addition, the IXCs, in order to recover these costs, have to surcharge the millions of parties responsible for paying for the underlying call from the payphone. This creates the very same type and magnitude of transaction costs as the set use fee approach, an approach which (as discussed above) the Commission rejected on the very ground that it resulted in excessive transaction costs. An added complication is the Commission's requirement that facilities-based carriers track and compensate on behalf of switchless resellers. PSPs may look to a reseller for compensation, when in fact the reseller's underlying carrier has already paid for the reseller's calls. Or, the PSP may expect more from a facilities-based carrier that it is really due, because some of the calls the PSP perceives as being handled by that carrier are in fact attributable to a switch-based reseller that is compensating the PSP directly. Avoidance of these complications and

[13] See Greater Boston Television Corp. v. FCC, 444 F.2d 841, 852 (D.C. Cir. 1970), cert. den. 403 U.S. 923 (1971).

transaction costs is a clear benefit for switching to a caller pays approach.

A second benefit from caller pays is consistency with the Commission's approach to local calls. If the Commission believes that the market can effectively set proper rates for local calls, then there is no reason to employ a different approach to other calls that a user chooses to make from a payphone as well.

Third, any Commission-prescribed rate will inevitably lead to continued burdens on the Commission's (and the private parties') resources, not only in the initial litigation of the reasonableness of the prescribed rate, but in resolving payment disputes between PSPs and carriers, and also in considering the requests that inevitably will arise from time to time to alter the prescribed rate because of changes in circumstances.

The Court's decision in Payphone II quite clearly calls on the Commission to take a new approach to payphone compensation. If the Commission wishes to utilize a market-based compensation plan – a possibility that the Court left open – then Sprint believes the Court is likely to be receptive to the only real market-based option open to the Commission: a caller pays plan.

In that regard, Sprint believes the Commission is foreclosed from attempting to fashion a market-based compensation plan under a carrier-pays scheme. In the first place, as the court correctly noted in Payphone II (at 3), "[n]o discernible 'market rate' for coinless payphone calls actually existed… ." This necessarily leaves the Commission in the position of "prescribing" a "market-based" rate – a concept that is inherently an oxymoron. If there truly were a market, there would be no need for a Commission-prescribed rate (or rate formula). Conversely, the very fact that the Commission prescribes a carrier-pays rate means that the rate is not established by the market. The problems and the nine-figure costs involved in attempting to develop the selective call blocking systems that would be required to give IXCs the same ability that callers have to "walk away" from a phone – i.e., to be able to reject a call from a particular payphone to a particular access code or subscriber 800 number – are well documented in the record.[14] Such systems are not available now, will not be available in the near future, but would be essential to give IXCs some measure of bargaining leverage with PSPs. Without such systems, and so long as the IXCs are under a legal compulsion to pay something to the PSPs for payphone-originated calls, there can be no genuine market-determined rate between carriers and PSPs.

What little evidence there is of the free interplay of market forces between IXCs and PSPs, however, suggests that the market rate would be very low indeed. Before §226 was enacted, market conditions did exist as between IXCs and independent payphone providers (IPPs). IPPs were not legally prohibited from blocking either access code calls or subscriber 800 calls, and IXCs were under no legal compulsion to compensate IPPs for either category of calls. Some IPPs did block access code calls, but no IXC paid IPPs to unblock such calls, as far as Sprint is aware. Thus, it could be reasonably said that the only true "market" rate was zero. After §226 was enacted, IPPs were prohibited from blocking access code calls (but not subscriber 800 calls), and IXCs were compelled by the Commission to compensate IPPs for access code calls. It may be noted that in mid-1994, AT&T (by far the largest IXC) and American Public Communications Council (APCC) (a trade association representing the vast majority bulk of the IPP industry) did

[14] See e.g., the August 26, 1997 comments of AT&T (at 16-17); and Cable & Wireless, Inc. (at 10-11).

agree to a $.25 rate for access code calls, in lieu of AT&T's share of the Commission-mandated rate of $6.00 per line per month.[15] At that time, AT&T did not volunteer to pay any compensation for subscriber 800 calls, and APCC had no assurance that it would ever be able to receive any compensation for subscriber 800 calls.[16] Thus, it could be again inferred that the market rate for subscriber 800 calls was zero, since APCC's members were free to block such calls if they wished to develop the capability to do so, and APCC and AT&T had not negotiated any compensation for such calls.

Another indication of what a carrier-paid market rate might be for the calls in question was described at pp. 12-14 of AT&T's September 9, 1997 Reply Comments. There, AT&T adjusted the $.25 rate applicable to dial-around operator service calls that APCC had agreed to, to reflect the far lower value (to IXCs) of subscriber 800 calls and to reflect the fact that most of the calls at issue here are subscriber 800 calls. These adjustments resulted in a rate of 10.67 cents per call. Simply as means of avoiding further litigation, such a rate would be acceptable to Sprint. Furthermore, such a rate would, if anything, be a generous carrier-paid market-based rate for payphone providers, since it includes some allowance for subscriber 800 calls (for which PSPs have never been able to negotiate any compensation from IXCs) and reflects a $.25 per call rate for dial-around calls that was not the product of a free negotiation, but was offered by AT&T

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[15] The Commission subsequently granted AT&T a waiver to implement this negotiated rate. Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, 10 FCC Rcd 1590 (CCB, 1994). Later, Sprint also received a waiver to pay the same rate, although it had never negotiated or reached agreement with APCC (id., 10 FCC Rcd 5490 (CCB, 1995)).

[16] Their agreement was entered into at a time when the Commission viewed §226 as precluding compensation for such calls, a decision that was later remanded to the Commission in Florida Public Telecommunications Assn. v. FCC, 54 F.3d 857 (D.C. Cir. 1995), which was decided roughly a year after the AT&T/APCC agreement.

only as an alternative to its share of the Commission-prescribed $6.00 per line per month. Nonetheless, it is not a true market rate, since it is not the product of truly free negotiations between IXCs and PSPs. And, as indicated above, the very notion of a Commission-prescribed market rate is an inherent contradiction in terms.

Finally, adoption of a caller pays plan would not preclude the possibility of a carrier-pays market from developing in the event that such a possibility is realistic. If, for example, a carrier believes that the caller pays plan is unduly dampening demand for calls that the IXC would otherwise receive and handle (whether access code calls or subscriber 800 calls or both), a caller pays approach would not preclude that carrier from negotiating with PSPs to allow such calls to be made without advance payment, subject to some appropriate and mutually agreed upon compensation between the carrier and the PSPs. But it is only when IXCs are no longer compelled to compensate PSPs as a matter of course, and PSPs are free to look elsewhere – to the calling party – as a source of compensation, that a market between IXCs and PSPs could even possibly emerge.

III. CARRIER PAID COMPENSATION SHOULD BE BASED ON A COST-BASED RATE

If the Commission chooses not to adopt a market-based caller pays plan for payphone compensation, then the only logical alternative is to prescribe a cost-based rate. As Sprint has explained in its earlier filings,[17] the Commission has a long history of basing rates in regulated multi-provider markets on the costs of the most efficient (or "bellwether") provider, on the basis that the Commission has no duty to ensure that each provider will earn a fair return on its investment,[18] and that even using industry average

[17] See e.g., Comments of Sprint Corporation on Remand Issues, August 26, 1997, at 5-8.

[18] See Postal Telegraph-Cable Company et al., 5 FCC 524-527 (1938).

costs would reward less efficient or less competent operators and would thus deprive the public the benefit of competition.[19] The Commission already has sufficient cost data, from a representative segment of efficient payphone providers, to proceed to establish a cost-based rate.[20]

First, the Commission has data showing that Bell Atlantic's payphone costs in Massachusetts for local coin calls amount to 16.7 cents per call.[21] Even accepting the Commission's prior and substantially understated estimate that the cost difference between a local coin call and a coinless call is 6.6 cents per call,[22] the Bell Atlantic-

[19] See The Western Union Telegraph Co., 25 FCC 535, 580 (1958). As Sprint explained (see n.17, supra) the Commission continued to use the bellwether concept into the 1980s, until the Commission ceased to regulate rates of nondominant carriers.

[20] In the Second Report and Order, the Commission performed an alternative cost study (that it specifically disclaimed relying on). However, that study was based solely on selective cost data for IPPs, and those costs were far above the costs of LEC PSPs (who account for the vast majority of the payphones in service). This clearly violated (without explanation) the long-standing bellwether policies of the Commission. In these remand proceedings, the Commission should view with deep suspicion any new cost data from the RBOCs. All along, they have known what their costs are and have had multiple opportunities to present such data, but have not done so, whereas the IXCs have no systematic access to such data and can introduce such data only if and when it becomes available to them. The only reasonable inference that can be drawn by their failure to produce such cost data in the past is that such data would lead to far lower rates than the Commission has prescribed. It would not be surprising if the RBOCs were to introduce concocted and inflated cost studies now in an attempt to provide alternative grounds for the unconscionably high rates they seek.

[21] See Comments of Sprint Corporation on Remand Issues, August 26, 1997, Attachment A. The RBOC/SNET/GTE Payphone Coalition ("RBOCs"), on behalf of Bell Atlantic, previously claimed that this cost represented incremental costs (without explaining or defining its use of that term) and thus sought to discourage the Commission from relying on these costs. However, the RBOCs refused to submit the underlying cost study for examination by the Commission and interested parties, and thus any attempt by the RBOCs to characterize this cost study must be disregarded by the Commission on the basis of the "best evidence" principle. See Reply of Sprint, October 6, 1997, at 1-2.

[22] AT&T demonstrated, in its December 1, 1997 Petition for Reconsideration (at 17-20), that the Commission's estimate failed to deduct the profit on the avoided costs (which

Massachusetts costs for coinless calls would amount to only 10.1 cents per call for its 45,000 payphones.

Second, Sprint introduced evidence showing the fully allocated costs of its LECs' payphone operations,[23] which encompass 50,000 payphones. That data shows, based on the Sprint LECs' actual usage, a per-call cost for coinless calls of 16.9 cents, without any deductions to reflect the cost of local call completion that is avoided in access code/subscriber 800 calls, and maintenance expense and depreciation related to the coin mechanism. Ignoring maintenance costs altogether,[24] and using the Commission's allowances of 3.1 cents per call for depreciation of the coin mechanism and 2.75 cents for local call completion, would result in a coinless call cost for the Sprint LEC payphones of 11.05 cents per call.

Third, AT&T, in its December 1, 1997 Petition for Reconsideration, submitted payphone cost data for Southwestern Bell's payphones. These data, which relate to roughly 190,000 payphones (see Attachment 1 to Affidavit of David C. Robinson,

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AT&T did not quantify), understated local call completion costs by 2.25-5.25 cents per call, and overstated the added cost of Flex ANI digits by at least .9 cents per call. See also, Opposition of Sprint for Petitions for Reconsideration, January 7, 1998, at 4-12. In addition, the Commission's allowance to PSPs of .8 cents per call to reflect the time lag in receiving payment from IXCs after a call is made (13 FCC Rcd at 1805-06) was excessive, since it was based on a full 11.25% return on investment rather than the short-term cost of money. See Sprint's May 4, 1998 Petition for Reconsideration in this docket. As further proof that the Commission's estimate of local call completion costs was too low, it was recently reported that the Delaware PSC set measured usage rates for local calls on payphone lines at $.03 for the first three minutes and $.005 for each additional minute, which would translate to a total of 5.5 cents on an eight minute call. See "Putting It To The Test," Perspectives, July 1998, at 21.

[23] See Reply of Sprint Corporation on Remand Issues, September 9, 1997, Exhibit 1.

[24] The Commission found (13 FCC Rcd 1803-04, n.145) that it was difficult to separate maintenance costs from coin collection costs, and the Sprint study did reflect a deduction for coin collection costs.

appended to AT&T's petition), after adjustments agreed to by AT&T on reply,[25] show a cost for coinless calls of between 15.9 and 16.4 cents, even using the unduly conservative costs estimated by the Commission in its Second Report and Order for local call completion and coin collection and maintenance.

The Commission would be fully justified in prescribing a rate of 10.1 cents per call using Bell Atlantic-Massachusetts as a bellwether. However, taking an average of the three LECs' costs, weighted by the number of payphones (and using the midpoint of 16.15 cents per call for Southwestern Bell's costs) would result in a rate of 14.3 cents per call[26] that would be acceptable to Sprint.

IV. CHANGES IN THE PAYPHONE MARKET SINCE THE SECOND REPORT AND ORDER DO NOT SUPPORT USE OF LOCAL COIN RATES LESS COST DIFFERENCES BETWEEN COIN AND COINLESS CALLS

As indicated at the outset, the June 19 Public Notice raises a number of questions that appear designed to elicit support for the Commission's twice-rejected determination to use the local coin rate as a starting point for establishing payphone compensation. The Commission would be ill-advised to consider such an approach again. Apart from the fact, discussed in Section II above, that the very concept of a Commission-prescribed market rate is an inherent contradiction, the use of the local coin rate (even if it could be assumed that this rate approximates the cost of a local coin call) to determine a market-based rate for IXC-paid compensation is fundamentally illogical. As has been well-

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[25] See AT&T Reply, January 20, 1998, reply affidavit of David C. Robinson at ¶13.

[26] [(10.1 x 45,000) + (11.05 x 50,000) + (16.15 x 190,000)] / 285,000 = 14.3.

documented on the record,[27] the two markets are so different that the market rate for one market cannot be determinative of the market rate in the other, any more than the price of a stripped-down, basic automobile can be inferred from looking merely at the price of a luxury car built on the same chassis and the differences in the production costs of the two vehicles.

In any event, the local coin rates do not reflect underlying economic costs. Rather, that market continues to be characterized and indeed driven by the monopsony power of premises owners. In a typical competitive market, competing entities vie for the favor of those who use their product by offering the best possible service at the lowest possible price. That has not been and is not likely to be the case with competition in the payphone market. Rather, PSPs focus not on currying favor with callers, but on gaining exclusive contracts with premises owners to place their payphones on the premises. They do so by promising ever-higher commission payments to premises owners.

Since the Second Report and Order was issued – and since deregulation of rates for local coin calls became effective – the rates for these calls have swiftly risen to the $.35 rate the Commission had previously anointed as "market-based," regardless of underlying economic costs. Indeed, as shown above in Section III, the actual costs for local coin calls are substantially less than that level. Two PSPs have publicly admitted that this is what drives competition in the payphone market and thus has occasioned their rate increases to $.35. See U S West Communications Press Release, March 2, 1998, announcing a 40% increase in the local coin rate to $.35 in Idaho and stating that "to be

[27] See e.g., AT&T Reply, September 9, 1997, Attach. 3 (Declaration of Dr. Frederick R. Warren-Boulton); and AT&T Petition for Reconsideration, December 1, 1997, at 4-7.

competitive with these PSPs, we must pay market based commissions to our location providers to place our pay phones at their business. The only way to do this is to charge a competitive price to users of the phones." Similarly, in a July 1, 1998 press release by Bell Atlantic announcing an increase in local coin rates in Massachusetts from $.25 to $.35 – more than double its 16.7 cent cost – a Bell Atlantic spokesperson stated:

> We must pay competitive commissions to property owners to place our phones in their space... .
>
> We also must charge competitive prices to the users of our payphones... and the competitive price that has emerged nationwide is 35 cents for a local call.

Usually changing one's rates to charge a "competitive" price means lowering one's prices to meet competition, not raising them by 40%. Manifestly, the local coin rate has no relationship to the costs of making the phone available for local coin calls and keeping it properly maintained. Rather, the PSPs are escalating their rates without regard to costs so they can bid up the commissions they can promise to premises owners. There is only one reason why PSPs are bidding up he commissions they are offering to premises owners: the Commission has given them additional sources of money with which to do so.

Obviously, §276 was not enacted to make premises owners rich at the expense of the public. That is hardly what is meant by "fair" compensation. Thus, there is no warrant to accept as reasonable whatever commissions PSPs choose to pay to premises owners from their new-found revenues (both from local coin rate increases and from IXC-paid compensation on access code and subscriber 800 calls). As Dr. Frederick R. Warren-Boulton explained at pp. 7-8 in his declaration (see n.27, supra):

> Site rents thus reflect not the cost to the site owner (which may be negative, after taking into account benefits to the site owner from the presence of a pay phone – note that many site owners actually pay pay phone operators to install a pay phone on their premises) but rather the exercise of local monopoly power. Since, with competitive pay phone supply, payments to site owners reflect local monopoly profits, such payments are endogenous. Any regulatory mechanism that included these payments as part of the costs included in TELRIC would thus be simply validating the site owners' monopoly power. The result would be a spiral of prices chasing "costs." Inclusion of these "costs" in TELRIC raises the allowed price, thus increasing profits, which increases site payments, which justifies increase in price, etc.

The Commission properly excluded commissions expense from compensation for access code and subscriber 800 calls in the Second Report and Order, and should continue to do so.

In any event, the fact that local coin rates are rapidly escalating, not because of any underlying change in payphone costs but merely in response to the monopsony power of premises owners, is ample demonstration that there is no convergence between rates and costs in the local coin market.[28] However, even if there were, that could not cure the logical defect in attempting to set a "market" rate for coinless calls by subtracting cost differences from an entirely different market rate (whether cost-based or not). The only way to achieve similarity between the market segments for coin and coinless calls would be to adopt a caller pays plan for the latter as well as the former.

[28] In this regard, the Public Notice aptly points out (at 2) the limitation on the use of pennies in payphones as a factor that must also be considered. Since payphones typically do not accept coins of less than a nickel, even if it could be assumed (which is clearly not the case) that competition in the payphone market would drive local coin rates to approximate the costs of such a call, the rate would always be rounded up to the next highest nickel. This means that local coin rates always overstate costs.